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# ASB meeting minutes, 2004, December 14-16

American Institute of Certified Public Accountants. Auditing Standards Board

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**AUDITING STANDARDS BOARD (ASB) MEETING**  
**December 14-16, 2004**  
**Orlando, FL**  
*Approved Highlights*

**MEETING ATTENDANCE**

ASB Members

John Fogarty , Chair  
Harold Monk, Jr., Vice Chair  
Barton Baldwin  
Gerald Burns  
Craig Crawford (absent)  
George Fritz  
James Goad  
Daniel Goldwasser  
Lynford Graham  
George Rippey  
Lisa Ritter  
James Lee II  
Wanda Lorenz (except Tuesday)  
Keith Newton (except Wednesday)  
William Messier, Jr.  
Daniel Montgomery  
Diane Rubin  
Scott Seasock  
Michael Umscheid

AICPA Staff

Susan Jones, Director, International  
Richard Miller, General Counsel & Trial Board  
Chuck Landes, Director, Audit and Attest Standards  
Hiram Hasty, Technical Manager, Audit and Attest Standards  
Judith Sherinsky, Technical Manager, Audit and Attest Standards  
Sharon Walker, Technical Manager, Audit and Attest Standards

## Observers

Marcia Buchanan, *Government Accountability Office*

Julie Anne Dilley, *PriceWaterhouse Coopers LLP*

Bob Dohrer, *McGladrey & Pullen LLP*

Mary Ann White, *PPC*

Maria Manasses, *Grant Thornton*

Diane Hardesty, *Ernst & Young*

Jennifer Burns, *SEC*

## **AGENDA ITEMS PRESENTED AT MEETING**

### **1. SAS 60 – Communication of Internal Control Related Matters Noted in an Audit**

In March 2003, the Auditing Standards Board (ASB) issued an exposure draft of a proposed revision of Statement on Auditing Standards (SAS) No. 60, *Communication of Internal Control Related Matters Noted in an Audit* (AU sec. 325). After revising the SAS for certain matters noted in comment letters on the exposure draft, the ASB, at its September 2003 meeting, directed the task force to make conforming changes to the document to reflect certain definitions and related guidance in Public Company Accounting Oversight Board (PCAOB) Auditing Standard No. 2 (AS2), *An Audit of Internal Control Over Financial Reporting Performed in Conjunction with an Audit of Financial Statements*, and to send the revised draft to the ASB for a vote on final issuance. Michael Umscheid, chair of the Internal Control Task Force, led the Board in a discussion of a revised draft of SAS No. 60. The ASB directed the task force to:

- Use the ISA construct “those charged with governance” rather than audit committee
- Indicate that the report is always to management and the audit committee, or the equivalent of the audit committee
- Indicate that the requirements in this SAS are applicable in all audits.
- Provide an example of a compensating control in a small company in paragraph 6
- Amend paragraph 9 to indicate that although deficiencies in controls over procedures to record recurring and nonrecurring adjustments to the financial statements are common in small entities, if management decides that it will not implement such controls, the auditor should report such significant deficiencies to those charged with governance.
- Amend paragraph 9 to indicate that if management does not have the ability to prepare financial statements or certain aspects of the financial statements: (1) the auditor and management should acknowledge that deficiency in the engagement letter and should state that because of this deficiency the auditor will assist in

- preparing and adjusting the financial statements and (2) management should acknowledge this deficiency in its representation letter.
- Consider the options for situations in which the auditor identifies the same significant deficiencies and material weaknesses each year, and management chooses not to correct them.
  - Revise paragraph 13 to include that uncorrected significant deficiencies that have been communicated to management and the audit committee are indicators of an ineffective control environment if management ignores them, rather than assesses them and determines that they should not be addressed, for example, because of cost/benefit considerations.
  - Retain the references to a “reasonable person” in paragraphs 14 and 15.
  - Revise paragraph 27 to explain that it is the nature of the work performed in an audit (rather than the limited degree of assurance associated with the auditor issuing a written report) that is not sufficient to enable the auditor to conclude that no material significant deficiencies were noted during the audit. Also delete the reference to “written representations.”
  - Indicate that the reporting on internal control that is the subject of SAS No. 60 differs from that of AS2, for example, in SAS No. 60, the auditor is looking at a period of time rather than a point in time.
  - Revise the document to reflect the ASB’s comments so that the ASB can discuss the revised draft at its February 2005 meeting.

The ASB concluded that the document should be reexposed for comment because of the significant changes made since exposure.

## **2. Audit Documentation**

Mr. Graham, Chair of the Audit Documentation Task Force (task force), presented a marked draft of revised Statement on Auditing Standards (SAS) No. 96, *Audit Documentation*, to the Auditing Standards Board (ASB). Mr. Graham indicated that the draft was revised based on comments received from the Board following the September 2004 ASB meeting.

After discussion of the task force’s proposed revisions, the ASB directed the task force as follows:

- a. add that quantity, type and content of audit documentation are matters of the auditor’s professional judgment;
- b. not to include a requirement to prepare a concluding memorandum;
- c. add a requirement that the auditor document that the accounting records agree or reconcile with the financial statements or other information being reported on;
- d. make a conforming change to SAS No. 95, *Generally Accepted Auditing Standards*, to require the auditor to document his or her justification for a departure from the SAS in the workpapers.

The required changes were made to the proposed exposure draft and presented to the ASB for review.

The ASB approved the proposed exposure draft for a ballot vote.

### **3. Risk Assessment**

Mr. Darrel Schubert, co-chair of the risk assessments task force (task force), a joint project of the International Auditing and Assurance Standards Board (IAASB) and the ASB. See the appendix to these highlights for a description of the background of this project. Mr. Schubert led a discussion of the status of the project.

Mr. Schubert reported that the task force met on October 11, October 19 (via teleconference) and November 15, 2004 to discuss the following exposure drafts:

1. Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement (Assessing Risks)
2. Performing Audit Procedures in Response to Assessed Risks and Evaluating the Audit Evidence Obtained (Performing Procedures).

Mr. Schubert discussed the significant changes made to these exposure drafts since they were issued in December 2002. Significant changes were as follows:

1. Reflect comments arising from the comment letters. In total, there were thirty-one comment letters received.
2. Reflect revisions made by the IAASB to the International Standards on Auditing (ISA) exposure drafts in finalizing its International Standards on Auditing.
3. Reflect changes arising from the Public Company Accounting Oversight Board's (PCAOB), *Conforming Amendments to PCAOB Interim Standards Resulting from Auditing Standard No. 2, An Audit of Internal Control Over Financial Reporting Performed in Conjunction with an Audit of Financial Statements* of the PCAOB's conforming changes that may warrant conforming changes to SASs.
4. Other – Other revisions were made by the task force to better explain certain terms and reflect certain issues that have emerged since the exposure drafts and the ISAs were issued.

### **Future Actions**

At its meeting December 6-10, 2004, the IAASB approved the issuance of ISA 320 (revised), *Materiality in the Identification and Evaluation of Misstatements*. Mr. Schubert stated that the revised ISA 320 will impact the proposed SASs, *Audit Risk and Materiality* and *Performing Procedures* because, among other things, the sections,

Evaluating the Effect of Uncorrected Misstatements and Evaluation Whether the Financial Statements as a Whole are Free of Material Misstatement of the revised ISA 320 are currently covered in the Performing Procedures and need to be transfer to the Audit Risk and Materiality proposed SAS in order to align ISA 320 with the Audit Risk and Materiality exposure draft. Mr. Schubert also stated that the task force needs to assess what other revisions might be necessary as a result of the issuance of the revised ISA 320 exposure draft.

After discussion, the ASB concluded that all of the risk assessment exposure drafts should be re-issued for exposure. The plan is for the task force to discuss the risk assessment exposure drafts at the February 2005 ASB meeting and then deliberate a vote to re-expose all of the risk assessment proposed standards at the April 2005 meeting. Final standards would be issued in the Fall 2005, and would be effective for all audits beginning after December 31, 2006.

The next task force meeting is scheduled for January 11-12, 2005.

#### **4. Clarity**

Mr. Fogarty provided the ASB with an update on the IAASB Clarity project. In September 2004, the IAASB issued an exposure draft of a Proposed Policy Statement, *Clarifying Professional Requirements in International Standards Issued by the IAASB*.

The ASB agreed that staff would prepare an exposure draft for discussion at the February 2005 ASB meeting. The exposure draft would include use of terms and a discussion on implementation of the use of terms.

## **Risk Assessment Project Background Information**

On December 2, 2002 the ASB issued an exposure draft of a suite of seven proposed Statements on Auditing Standards (SASs) relating to the auditor's risk assessment process. The exposure draft consists of the following proposed SASs:

- *Amendment to Statement on Auditing Standards No. 95, Generally Accepted Auditing Standards*
- *Audit Evidence*, which would supersede SAS No. 31, *Evidential Matter* (AU sec. 326)
- *Audit Risk and Materiality in Conducting an Audit*, which would supersede SAS No. 47, *Audit Risk and Materiality in Conducting an Audit* (AU sec. 312)
- *Planning and Supervision*, which would supersede "Appointment of the Independent Auditor" (AU sec. 310), and SAS No. 22, *Planning and Supervision* (AU sec. 311)
- *Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement (Assessing Risks)*
- *Performing Audit Procedures in Response to Assessed Risks and Evaluating the Audit Evidence Obtained*, which would supersede SAS No. 45, *Substantive Tests Prior to the Balance-Sheet Date* (AU sec. 313), and, together with the proposed SAS *Assessing Risks* would supersede SAS No. 55, *Consideration of Internal Control in a Financial Statement Audit* (AU sec. 319)
- *Amendment to SAS No. 39, Audit Sampling*

In October 2003, the IAASB completed the international phase of the risk-assessment project by issuing the following three International Standards on Auditing (ISA):

- ISA 315, *Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement*
- ISA 330, *The Auditor's Procedures in Response to Assessed Risks*
- ISA 500, *Audit Evidence*.

In June 2004, the IAASB issued ISA 300 (revised), *Planning an Audit of Financial Statements*. In addition, on December 20, 2004, the IAASB has approved the issuance of the proposed exposure draft ISA 320 (revised), *Materiality in the Identification and Evaluation of Misstatements*.